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SUBJECT: IMF Recommendations for Algeria

1. Summary: In an October 16 press conference following a two-week visit to Algeria, Mr. Erik De Vrijer, Division Chief for Middle East and Central Asia at the IMF declared that Algeria showed favorable economic development in 2005. De Vrijer highlighted the "significant" structural reforms undertaken in 2005, including the association agreement with the EU, the new hydrocarbon law and the anti-corruption law. De Vrijer also made recommendations regarding the implementation of the economic revival plan, the salary policy and control of the banking system. END SUMMARY

FAVORABLE ECONOMIC PERFORMANCE IN 2005

2. Following a two-week visit to Algeria, Mr. Erik De Vrijer, head of the IMF delegation to Algeria and Division Chief in charge of Middle East and Central Asia, declared in a press conference that Algeria showed positive economic development in 2005. He affirmed that GDP growth remained around 5 percent, driven mainly by the hydrocarbon sector. The public works and services sectors demonstrated significant growth as well. He added that inflation was under control and unemployment would continue to decrease. "High oil prices will further reinforce the very good financial position of the country", De Vrijer said. In addition, he highlighted the structural reforms achieved by Algeria, in particular the association agreement with the EU effective since September first, the new hydrocarbon law that will help attract foreign direct investment, and the anti-corruption law.

"CAN DO BETTER"

3. The IMF chief of mission indicated that reforms had not been undertaken as rapidly as he would have liked. De Vrijer said that additional hydrocarbon resources generated by high oil prices gave more room for maneuver to the GoA in modernizing infrastructure and reinforcing human and institutional capital to support the private sector and create more jobs.

IMF RECOMMENDS CAUTION

4. De Vrijer recognized that the Algerian government's economic program targeted the increase of investment in key sectors and transition to a market economy, but he recommended caution in implementing new investment projects projected in the 2006 finance law to avoid spending more than the GoA should, and limit the impact of inflation. "The GoA should not speed up executing the program, otherwise it will face absorption problems and end up spending more than it should", he said. He also recommended limiting salary increases and adopting a salary policy aimed at preserving firms' competitiveness from external competitors. De Vrijer added that salary increases should be linked to non-hydrocarbon growth. Furthermore, he said it was time to think about eliminating tax exemptions and reducing employers' taxes to encourage investment and create growth within the formal economy.

MORE CONTROL ON BANKING SYSTEM LIQUIDITY

5. On the banking sector, De Vrijer argued for reinforcing the Bank of Algeria's control over liquidity. To minimize the inevitable cost of the association agreement with the EU, De Vrijer urged implementing banking reform, including privatization of public banks and cleaning up the financial arrangements between banks and enterprises. "The burden of non-performing loans is very heavy," said De Vrijer. To address the issue, the 2005 government budget included subsidies to state-owned enterprises reporting negative income, instead of directing state-owned banks to extend additional credit to cover the losses.

UGTA DENOUNCES IMF INTERFERENCE

16. Following De Vrijer's press conference, the General Union for Algerian Workers (UGTA) expressed discontent with his comments on salary increases. UGTA deemed them unacceptable and inappropriate. "He does not have the right to talk about salary policy in our country nor the labor market in the world. Algeria is no longer under the structural adjustment plan," said a senior UTGA official. The official said he intended to lodge a complaint against the IMF at its headquarters. The last salary increase was in 2003, when the GoA agreed to increase the minimum guaranteed salary by AD 2000 (\$27). The current minimum wage is \$137 a month.
ERDMAN